

USDA Agricultural Outlook Forum 2007

Transitioning Into A Common Sweetener Market With Mexico

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Presented: Friday, March 2, 2007



Topics for Discussion

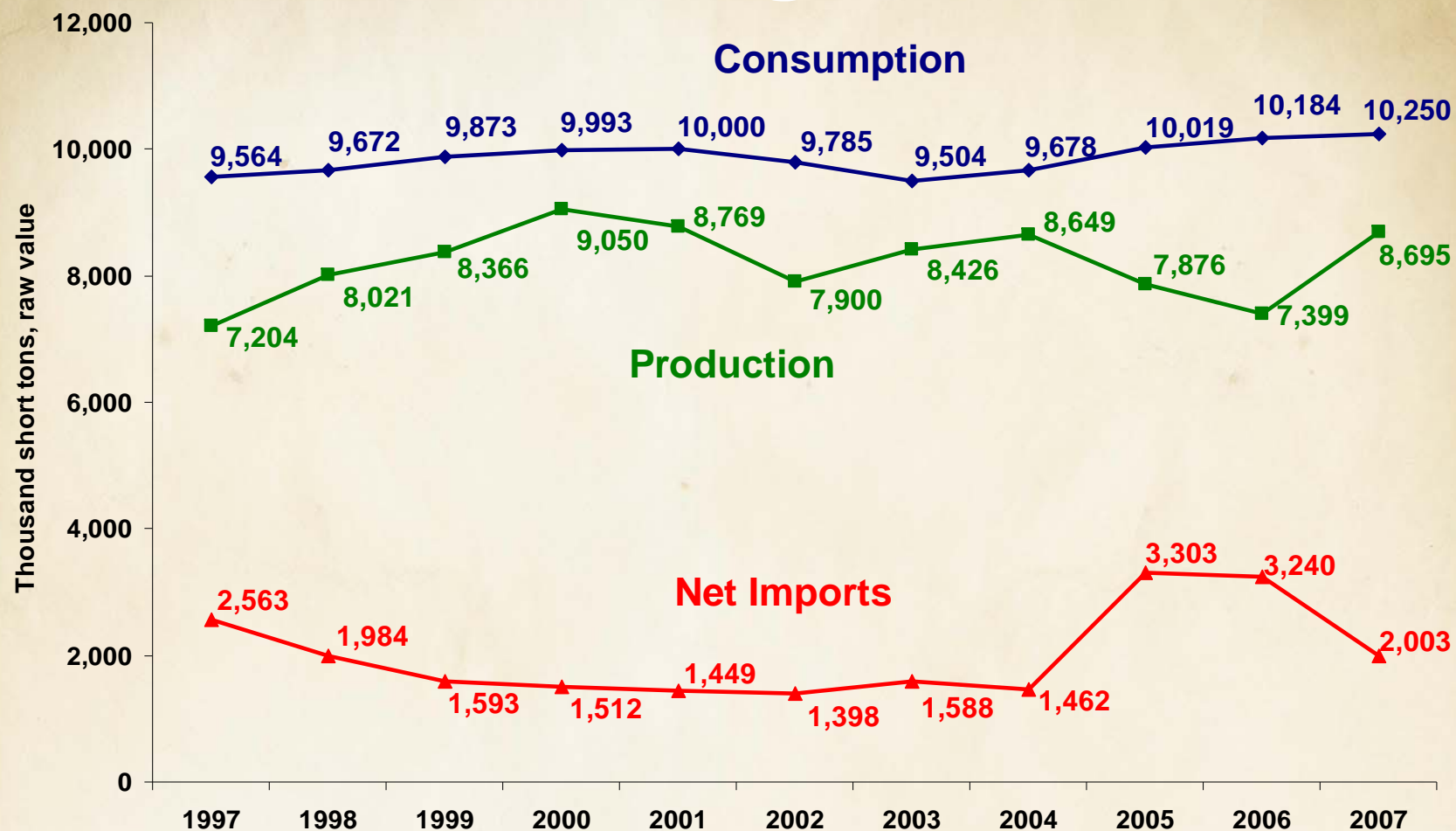
- Historical Market Perspectives
- What Could Cause A Joint Sweetener Market to Become Chaotic?
- Will Mexican Soft Drinks Convert to HFCS?
- Will the Merged Markets Be Out of Balance
- The Results



Historical Market Perspective

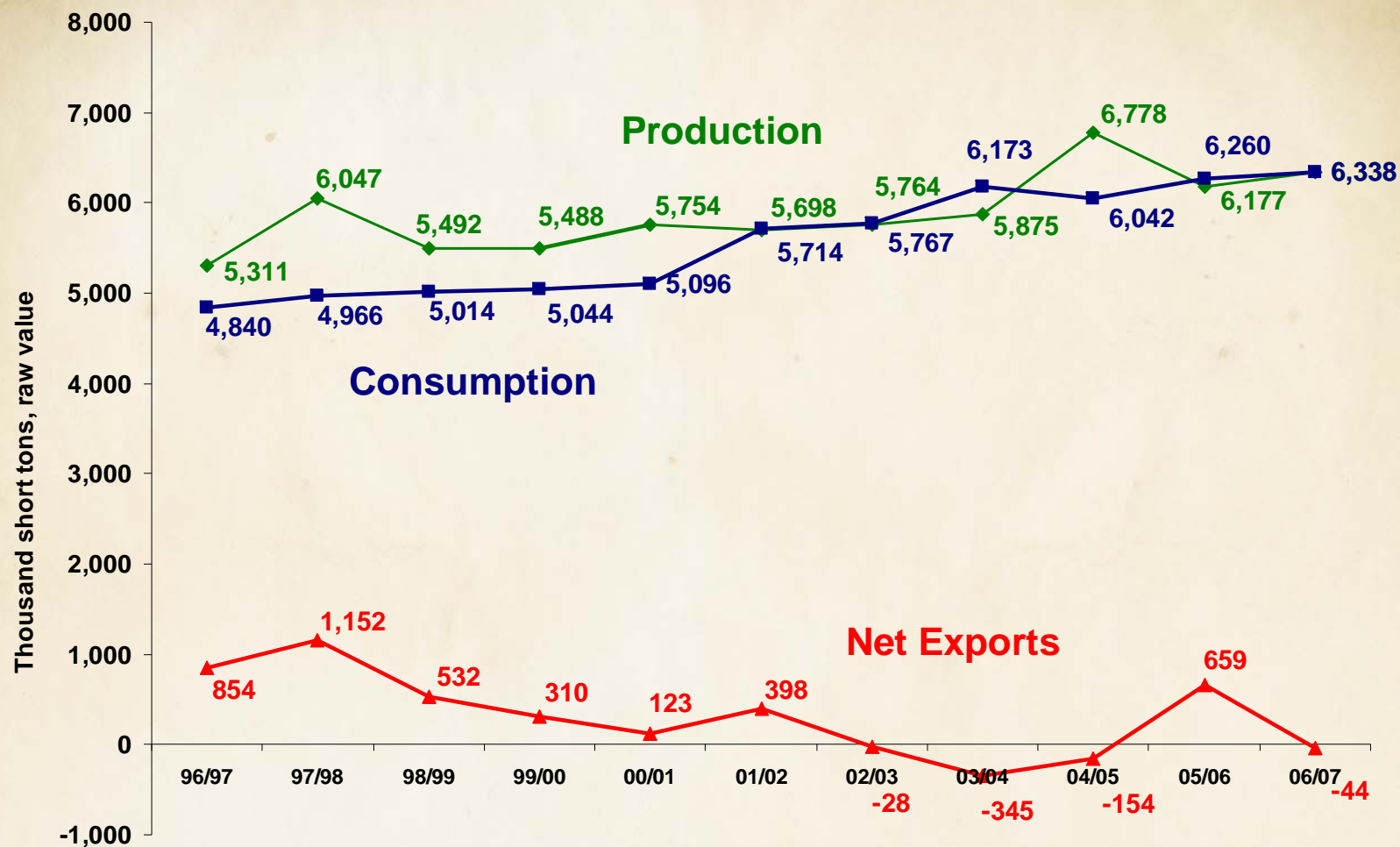
A faint, sepia-toned world map is visible in the background, centered behind the title text. The map shows the continents of North and South America, Europe, and Africa, with some internal borders and geographical features like rivers and oceans. The overall tone is historical and aged.

The U.S. Sugar Market



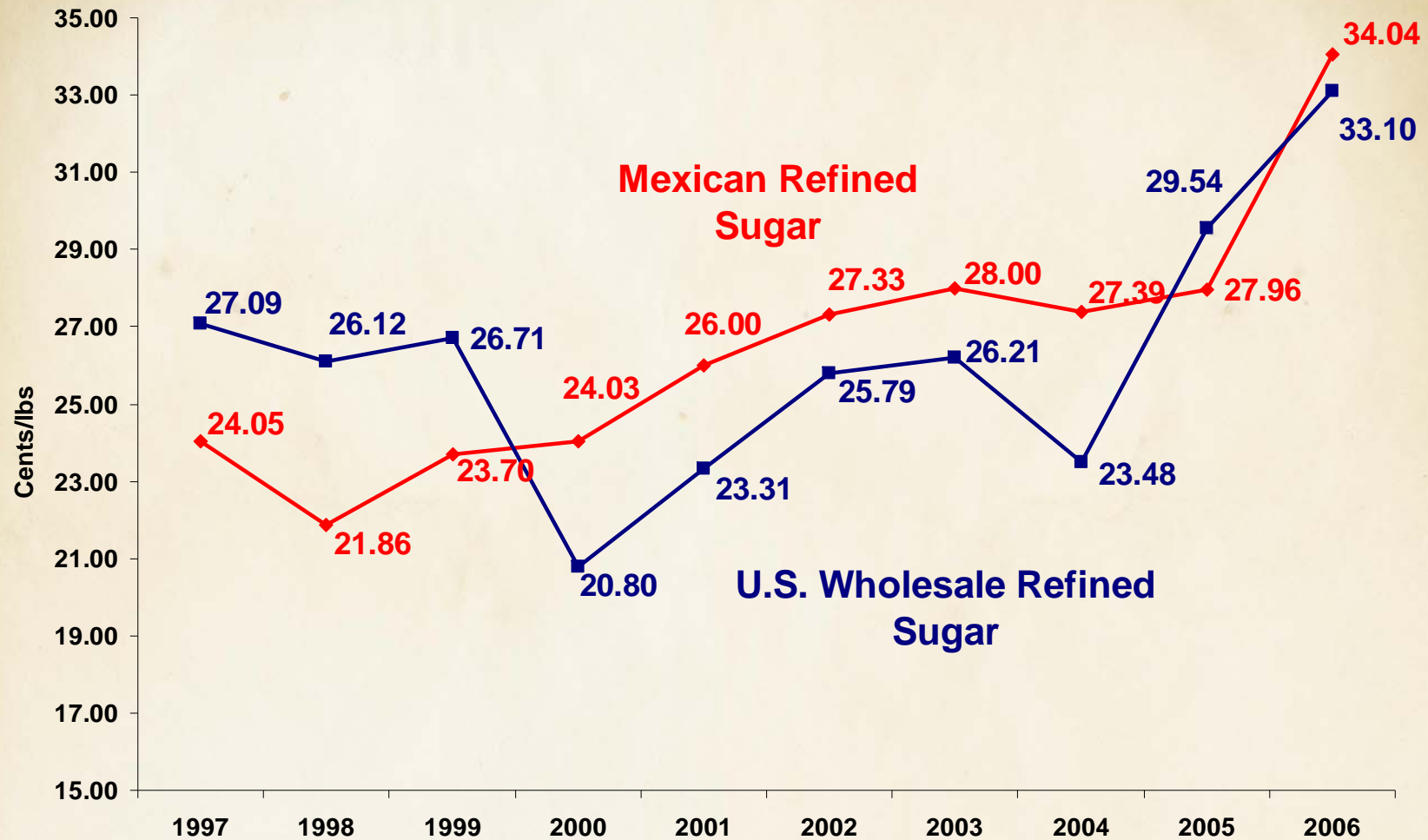
Source: USDA/ERS

The Mexican Sugar Market



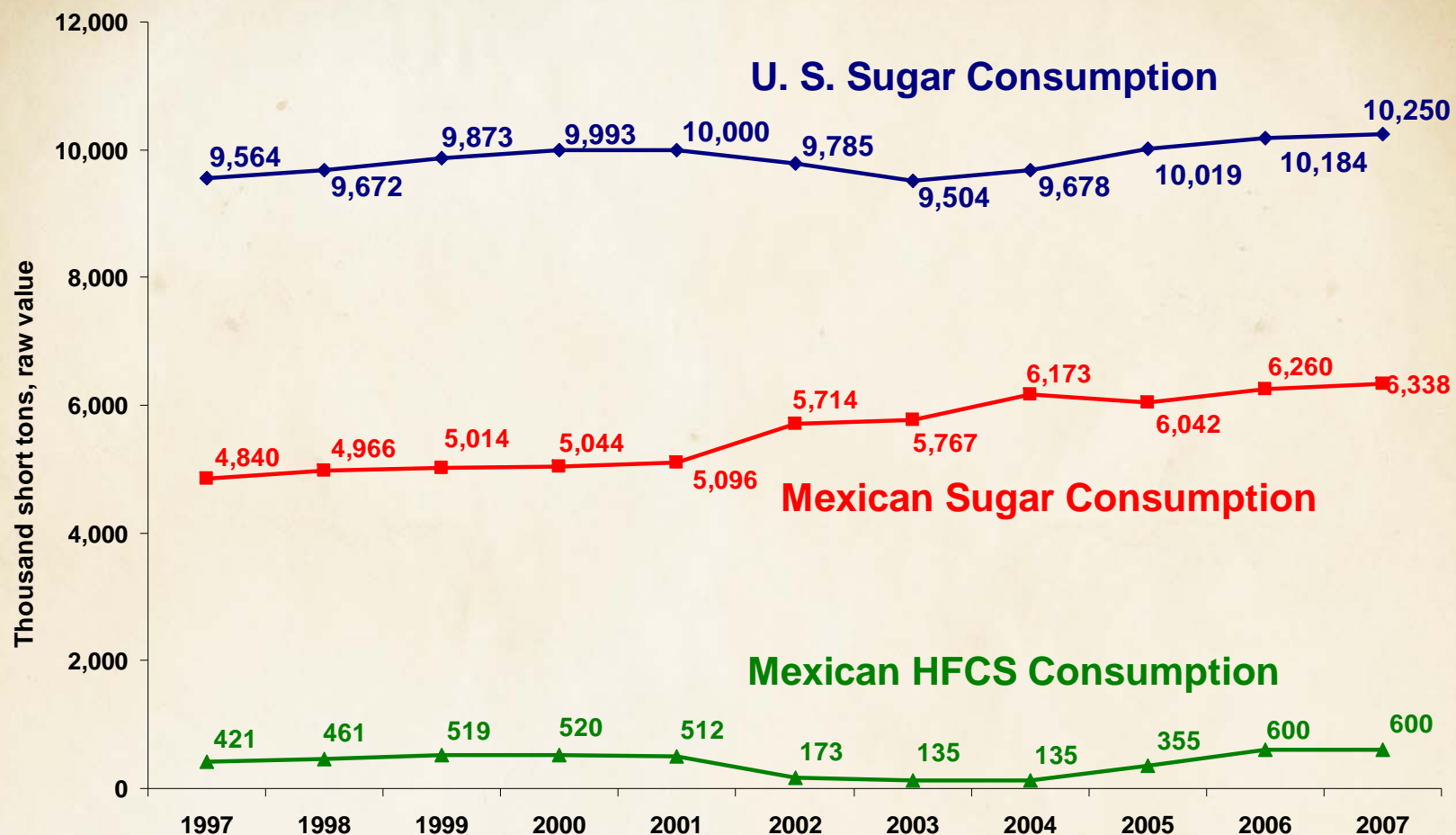
Source: USDA/FAS

Sugar Selling Prices In Mexico and The U.S.



Source: USDA and Servicio Nacional de Informacion de Mercados SNIM-ECONOMICA. January 3, 2007

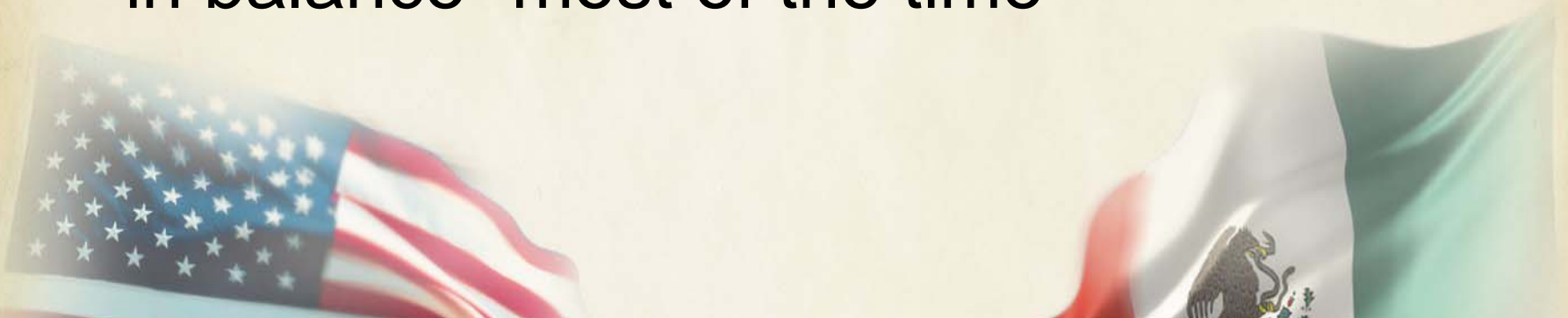
Sweetener Consumption Trends in Mexico and The U.S.



Source: USDA/FAS

Current Market Place Conclusions

- The Mexican and U.S. sweetener markets are growing
- Sugar selling prices have been steady to rising in both markets accentuated by major supply surpluses or shortages
- Sugar selling prices have, generally, been higher in Mexico than in the U.S.
- Both markets have, generally, been “in balance” most of the time



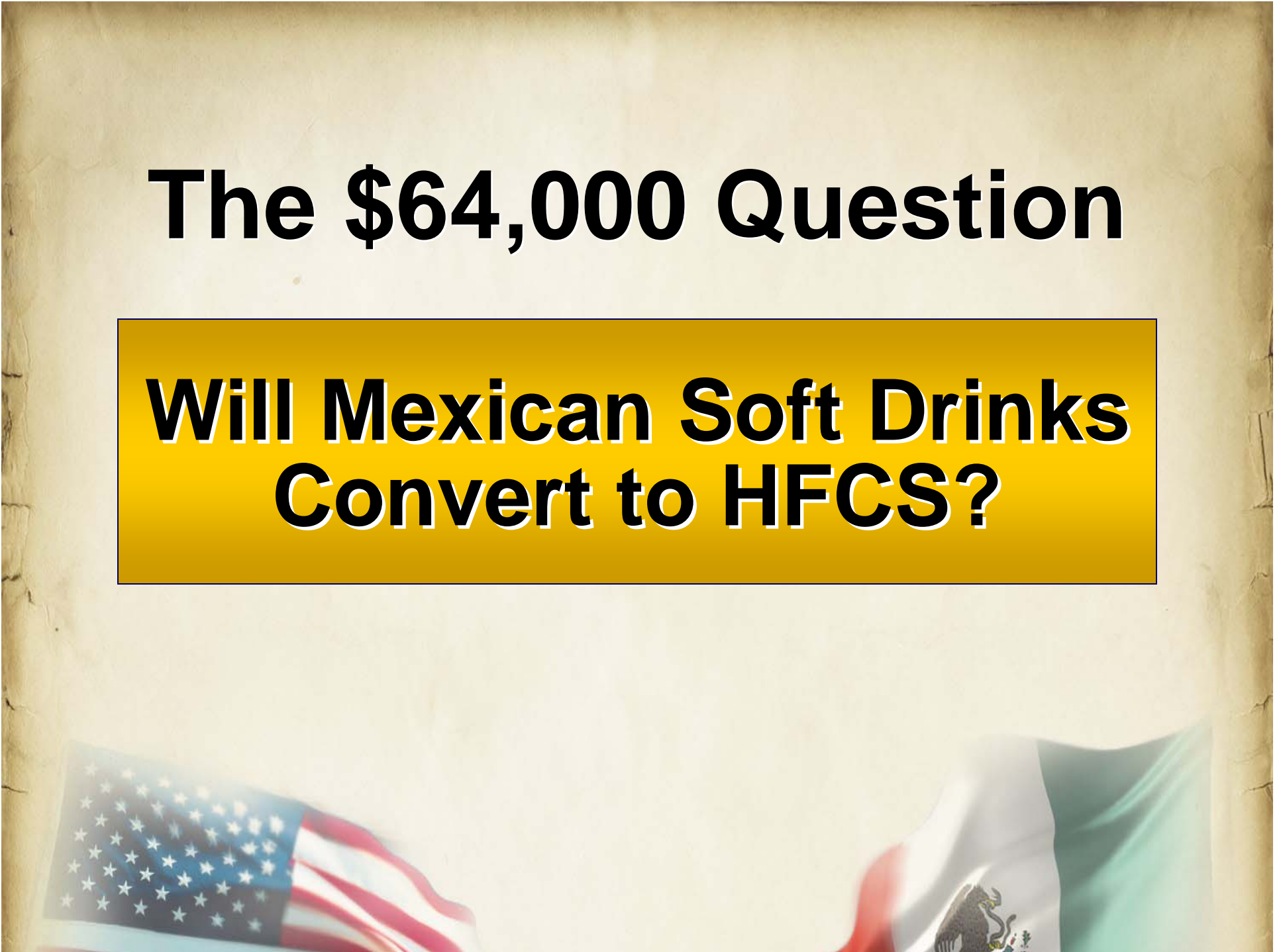
What Could Put The Mexican and U.S. Sugar Markets Into Disarray?

- Major decreases in consumption
 - Unlikely
 - Gradual growth is more likely
- Major increases in production
 - Unlikely
 - Gradual increase is probable
- New/Different sweetener use patterns
 - Major change in HFCS use in Mexico



The \$64,000 Question

**Will Mexican Soft Drinks
Convert to HFCS?**

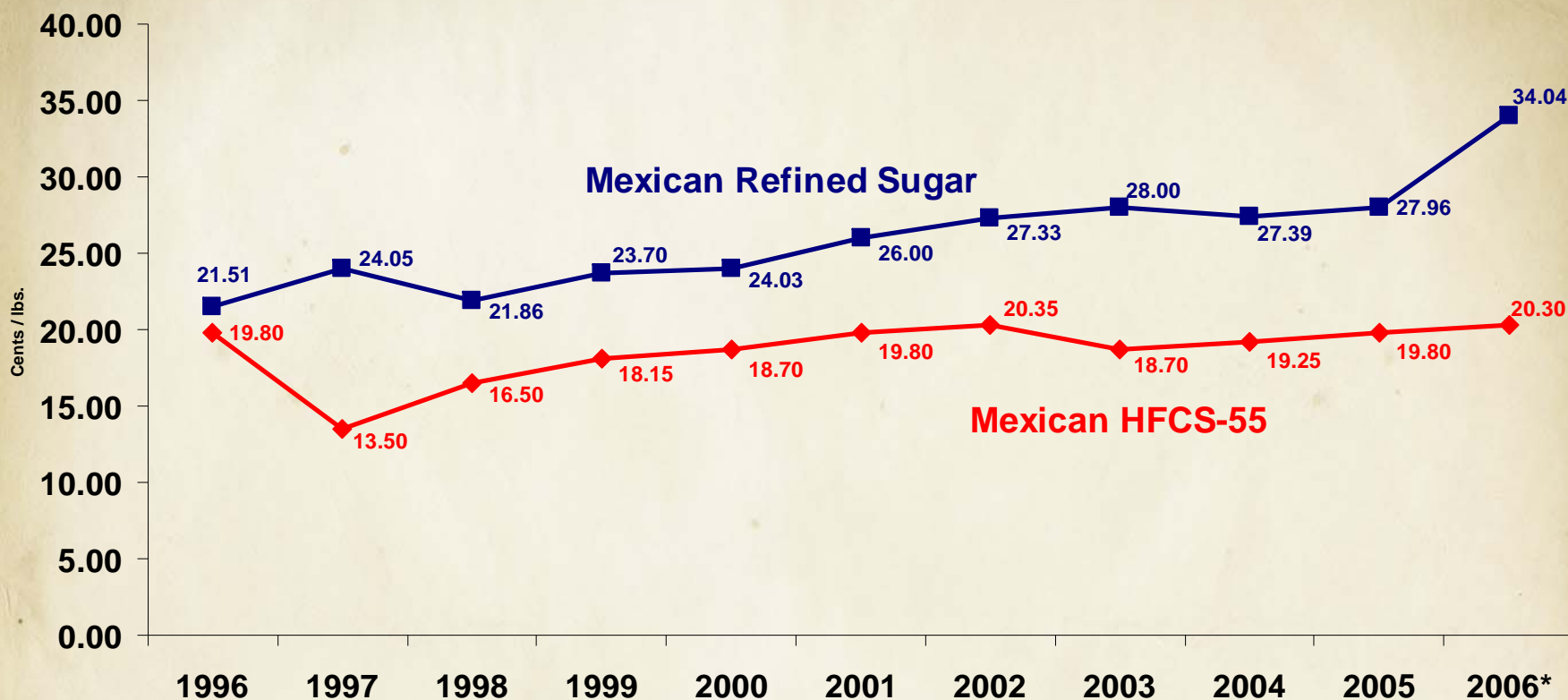


High Fructose Corn Syrup Use in Mexico and the U.S.

- HFCS now sweetens nearly all caloric soft drinks in the U.S. since a conversion from sugar in the mid-1980's
- Sugar now sweetens nearly all caloric soft drinks in Mexico
 - Estimated at 1.5 to 2.0 million tons



Will The Mexican Caloric Soft Drink Segment Convert to HFCS?



*Projections

Source: Sugar - Servicio Nacional de Informacion de Mercados SNIIM-ECONOMICA, HFCS-55 (dry equivalent basis) - McKeany-Flavell.

**Will The Mexican Caloric
Soft Drinks Segment
Convert to HFCS?**

**Economics
Rules!**



Will The Mexican Caloric Soft Drinks Segment Convert to HFCS?

- Potential Limiting Factors
 - HFCS Production in Mexico is small
 - 250,000 tons
 - U.S. “swing capacity” is making ethanol
 - Corn prices are rising – effect on HFCS prices
 - U.S. annual “excess” capacity for HFCS is estimated at 250,000 to 500,000 tons
 - U.S. seasonal “excess” capacity for HFCS is zero for significant portions of the year



Will The Mexican Caloric Soft Drink Segment Convert to HFCS?

- Marketing questions:
 - Would the Mexican palate “accept” HFCS?
 - Would a blend of sugar and HFCS be more acceptable?
 - Would seasonal changes in sweetener be acceptable?
 - Would more HFCS production capacity be built in either Mexico or the U.S. or both?

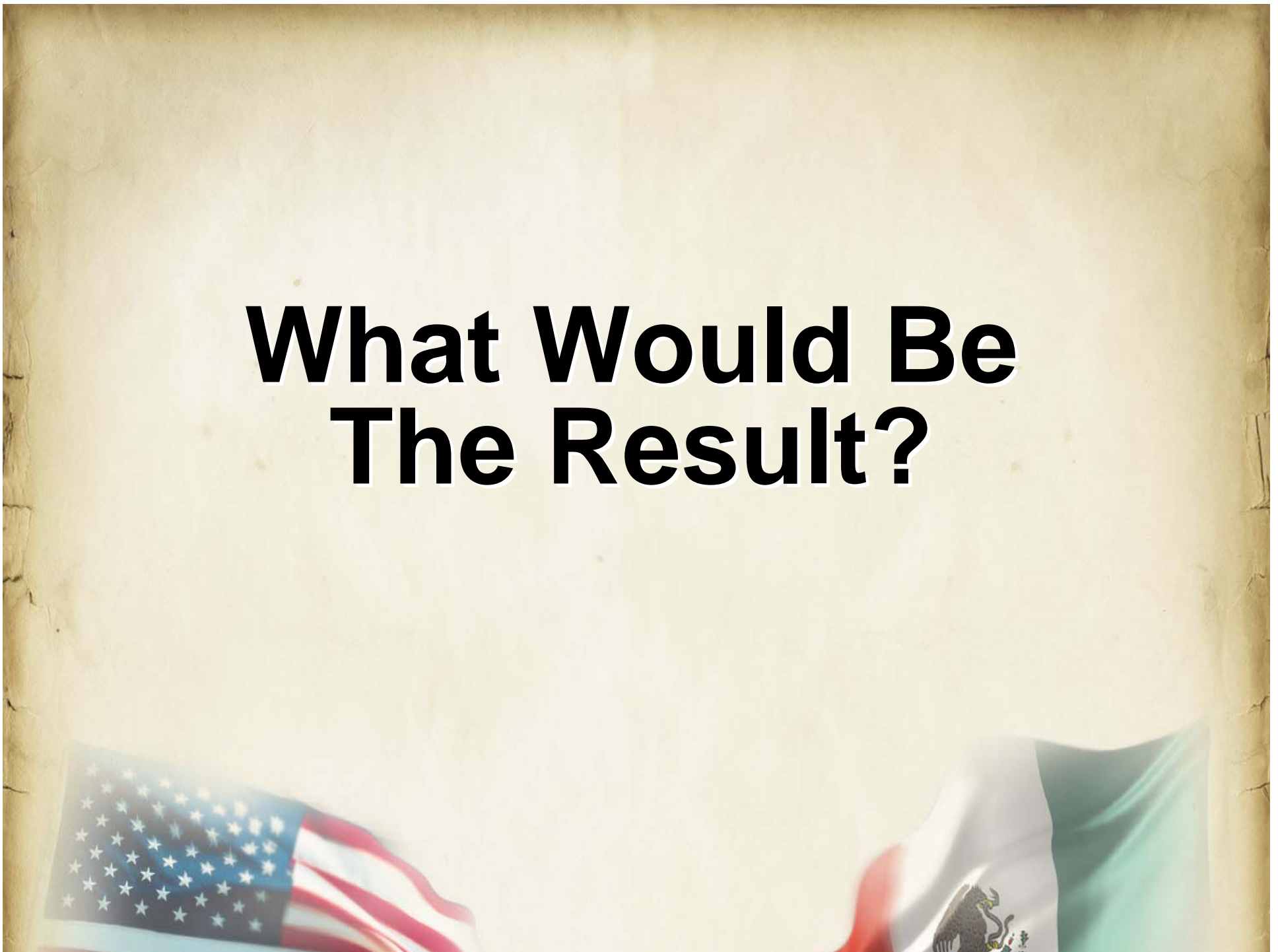


Conclusions

- If the soft drink industry in Mexico converted to the use of HFCS, the combined Mexican/U.S. sugar industry would become out of balance with existing supply pursuing significantly reduced demand.



**What Would Be
The Result?**



The Result

- With open borders, displaced Mexican sugar would move to the U.S. market
 - Prices in the U.S. market would fall
 - Forfeitures
- With open borders, displaced U.S. sugar would move to the Mexican market
 - Prices in the Mexican market would fall
 - More exports to the U.S.
- Downward price spiral!



Multiple Options Emerge

- Mexico could again close its borders to HFCS
 - Peace and tranquility return to sugar markets
 - U.S. HFCS manufacturers lose
 - Sustainable?
- Mexico could close its borders to U.S. sugar
 - The U.S. would retaliate by closing its borders to Mexican sugar
 - HFCS manufacturers are pleased
 - U.S. sugar producers are pleased
 - Mexican sugar industry loses



Multiple Options Emerge

- There is rationalization in the Mexican and U.S. sugar industries until balance is restored
 - HFCS manufacturers are winners
 - U.S. and Mexican sugar industries are losers
 - Customers are losers – less reliable sugar markets in both countries, higher cost supply chain



Multiple Options Emerge

- Anti-Dumping/Countervailing Duty Cases are successful
 - Significant portion of the Mexican sugar industry is owned by the Mexican government
 - What more would the Mexican government do to “protect” its “million person” sugar industry?
 - Costly legal battles follow proven “damages”



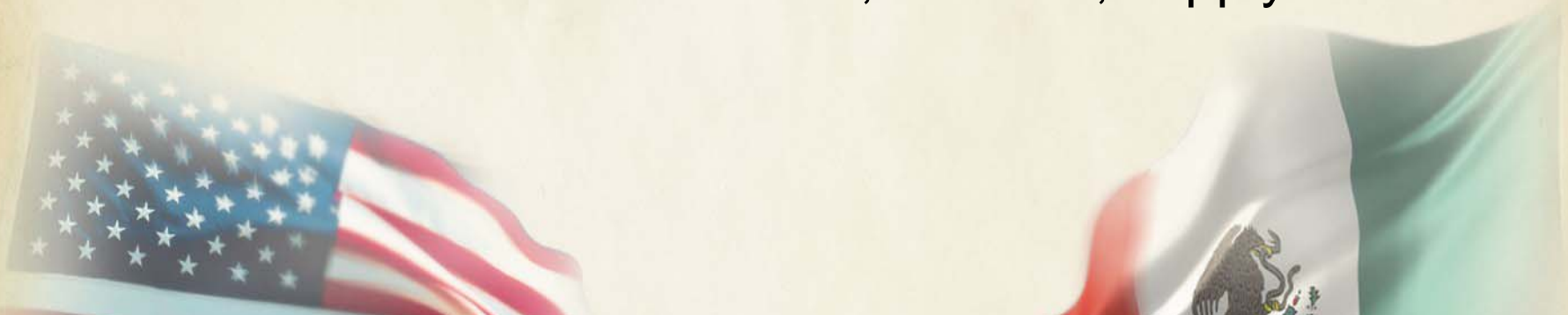
Multiple Options Emerge

- Might an ethanol industry emerge to remove displaced sugar?
 - Depending on the price of gasoline, the economics aren't the best
 - U.S. energy independence goal



The Smart Solution

- A negotiated settlement may be achieved
 - Sweetener consumption growth in the combined market provides a win-win-win-win opportunity
 - HFCS gets “reasonable” access to Mexico
 - Mexican sugar gets “reasonable” access to the U.S.
 - The U.S. sugar market “absorbs” the increase
 - With time (growth), balance returns to the merged market
 - Customers have a reliable, low cost, supply chain



The Smart Solution

- The July, 2006, attempted settlement was a failed one
 - Low U.S. sugar prices (forfeitures?)
 - Tier II tariff in Mexico remains high
 - Long term issues were ignored
- A negotiated solution is inevitable
 - Stop the dislocation in the Mexican agriculture community
 - Stop forfeitures in the U.S.
- When will the two governments address this issue?



**“In preparing for battle
I have always found that
plans are useless, but
planning is
indispensable.”**

-- Dwight D. Eisenhower

